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E.O. 11652: N/A

TAGS: ETRD, EFIN, OECD, PO

SUBJECT: OECD CONSULTATIONS ON PORTUGUESE IMPORT
SURCHARGE JULY 11

1. SUMMARY: IN BACK-TO-BACK SESSIONS OF ECONOMIC AND DEVELOPMENT REVIEW COMMITTEE AND TRADE COMMITTEE WORKING PARTY JULY 11, PORTUGUESE DEL PORTRAYED PRESENT ECONOMIC DIFFICULTIES IN TERMS OF TRANSITIONAL PHASE IN WHICH PUBLIC SECTOR AND IMPORTS WERE HAVING TO MAKE UP FOR NEGATIVE EXTERNAL FACTORS AND TEMPORARY SHORTFALL OF PRIVATE DEMAND AND PRODUCTION STEMMING FROM CHANGES IN PORTUGUESE ECONOMIC/SOCIAL STRUCTURE. WHILE STRESSING ROLE OF IMPORT PRICE INCREASES AND WEAK FOREIGN DEMAND, PORTUGUESE RECOGNIZED IMPORTANCE OF NOT NEGLECTING SUPPLY CONSIDERATIONS IN POLICIES AIMING AT STABILIZING EXTERNAL BALANCE, INCLUDING NEED TO DEFINE PARAMETERS FOR PRIVATE SECTOR ACTIVITY--AN AREA IN WHICH DELEGATION STATED GOP HOPES TO MAKE PROGRESS THIS MONTH. PORTUGUESE ASSURED OTHER DELS THAT IMPORT SURCHARGE WAS NOT INTENDED TO HAVE LONGER RUN PROTECTIVE EFFECT. BOP DEFICIT, WHICH IS EXPECTED NEAR ESC. 30 BILLION THIS YEAR, WILL BE FINANCED OUT OF REMAINING EXCHANGE RESERVES AND FOREIGN LOANS, AND POLICY ON POSSIBLE FUTURE MOBILIZATION OF GOLD RESERVES IN 1976 OR LATER REMAINS UNDETERMINED. GENERAL THRUST OF COMMENTS BY SECRETARIAT AND OTHER DELS IN BOTH COMMITTEES WAS TO EXPRESS HOPE THAT MEASURES TAKEN BY GOP WOULD INDEED PUT ECONOMY BACK ON SOUND FOOTING, ESPECIALLY IN PRODUCTION AREA, WITHIN REASONABLE PERIOD OF TIME AND ENABLE REMOVAL OF SURCHARGE AT EARLY DATE. MISSION BELIEVES EXPERIMENT OF EDRD/TCWP COORDINATED COUNTRY EXAMINATION SET USEFUL PRECEDENT. END SUMMARY

2. GENERAL ECONOMIC REVIEW: OPENING STATEMENT OF PORTUGUESE DEL (CONSTANCIO OF BANK OF PORTUGAL AND GUIMARAES OF MINISTRY OF PLANNING) ATTRIBUTED COUNTRY'S LIMITED OFFICIAL USE

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GENERAL ECONOMIC PROBLEMS MAINLY TO HIGH INFLATION AND HIGH UNEMPLOYMENT, AGGRAVATED BY INCREASING IMPORT PRICES, DECREASING FOREIGN INVESTMENT, RETURNING SOLDIERS AND EFFECTS OF RECESSION ELSEWHERE ON TOURISM AND WORKERS' REMITTANCES (ALTHOUGH LATTER NOW RECOVERING). GOP RESPONSE WAS JOB-CREATING PUBLIC WORKS PROGRAM (ESC. 8.5 BILLION - 34,000 JOBS), SPECIAL ASSISTANCE FOR SMALL BUSINESS AND AGRICULTURE, AND PRICE CONTROLS

AND WAGE CEILINGS. TRADE DEFICIT FOR FIRST 4 MONTHS OF 1975 WAS ESC. 14.5 BILLION--DOUBLE 1974 LEVEL FOR SAME PERIOD--AND RESERVES AS OF JULY 2 HAD DECLINED BY ESC. 11.88 BILLION SINCE BEGINNING OF YEAR. DATA ON EMIGRANTS REMITTANCES WAS NOT COMPLETE BUT THESE SEEMED TO BE RUNNING SLIGHTLY ABOVE 1974 LEVEL.

3. OTHER DELS COMMENTS FOCUSSED ON FATE OF PRIVATE INVESTMENT IN PORTUGUESE ECONOMY, IMPACT OF SURCHARGE ON PRICES, OUTLOOK FOR AGRICULTURAL PRODUCTION AND INVISIBLES EARNINGS, EFFECT OF LARGE PUBLIC SECTOR DEFICITS, AND ROLE OF POLICY-INDUCED SUPPLY CONSTRAINTS AND WAGE INCREASES IN AGGRAVATING INFLATION AND WORSENING TRADE PERFORMANCE. US DEL MADE STATEMENT ALONG LINES OF REFTEL. SECRETARIAT INDICATED IT SUSPECTED GOOD DEAL OF SHORT-TERM CAPITAL OUTFLOW THROUGH OVER INVOICING OF IMPORTS AND UNDER INVOICING OF EXPORTS (WHICH ALSO MADE TRADE FIGURES LOOK WORSE). PORTUGUESE DEL SAID GOP RECOGNIZED PROBLEMS OF SHORT-TERM CAPITAL OUTFLOWS AND NEED TO CREATE MORE STABLE CLIMATE IN PRIVATE SECTOR. HE STATED GOP WANTED TO ESTABLISH

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PARAMETERS FOR PRIVATE SECTOR ON URGENT BASIS AND INTENDED TO MAKE CONCRETE DECISIONS ON THIS IN JULY. HE ALSO INDICATED A "CODE ON FOREIGN INVESTMENTS" WAS IN THE PLANNING STAGE. FINALLY, AN "ECONOMIC TRANSITION PLAN FOR 1976-78", READY BY THE END OF THE YEAR, WOULD SET PRIORITY DEVELOPMENT SECTORS. PORTUGUESE CALLED SECRETARIAT'S TOURISM PROJECTION FOR 1975 (FORECASTING STAGNATION OF RECEIPTS) OVERLY OPTIMISTIC IN VIEW OF WIDE-SPREAD CANCELLATIONS EXPERIENCED SINCE MARCH. IN AGRICULTURE SECTOR HE SAW MAIZE AS ONE BRIGHT SPOT (ACREAGE HAD INCREASED), WHILE FOR OTHER CROPS RESPONSE TO INCREASED CREDIT AVAILABILITIES AND RISES IN SUPPORT PRICES WAS EXPECTED TO BE SLOW.

4. RE PUBLIC DEFICIT, PORTUGUESE RECOGNIZED IT WOULD BE LARGE, BUT FELT IT WAS ESSENTIAL TO FILL GAP IN PRIVATE DEMAND AND THAT MONETARY CONSEQUENCES WOULD BE LIMITED IN VIEW OF SIZABLE BOP DEFICIT AND NEGATIVE MONETARY EFFECT OF BANKING OPERATIONS AT PRESENT. (IN

RESPONSE TO QUESTION, PORTUGUESE NOTED PROCEEDS OF IMPORT SURCHARGE WILL AUGMENT BUDGET REVENUES. THEY HAD NO PRECISE FIGURE, AND STATED THAT ESC 5 BILLION ESTIMATED PROCEEDS FOR 6 MONTH LIFE OF SURCHARGE TOO HIGH BECAUSE (A) PROJECTED AT NO CHANGE IN IMPORT VOLUME AND (B) DID NOT TAKE INTO ACCOUNT AD HOC EXEMPTIONS ALLOWED FOR GOODS COVERED BY SURCHARGE.) IN RESPONSE TO POINTED GERMAN SUGGESTION THAT ROOT CAUSE OF PORTUGUESE EXTERNAL PROBLEM WAS HIGH INTERNAL INFLATION AND DISRUPTION IN PRODUCTION (MAKING IT HARD TO EXPORT AND STIMULATING IMPORTS), PORTUGUESE DEL NOTED GOP FULLY AWARE OF SUPPLY PROBLEM (E.G. IT HAD CALLED FOR A "BATTLE OF PRODUCTION") AND POINTED TO WEAK FOREIGN DEMAND AND RISING IMPORT PRICES AS EQUALLY IMPORTANT FACTORS. ALTHOUGH COST OF SURCHARGE COULD BE PASSED THROUGH TO PRICES TO CONSUMERS, SURCHARGE WAS EXPECTED ON BALANCE TO HAVE BENEFICIAL DAMP LIMITED OFFICIAL USE

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ENING EFFECT ON NON-ESSENTIAL CONSUMPTION.

5. FINANCING DEFICIT: PORTUGUESE DEL SAID THAT ESTIMATED BOP DEFICIT OF 30 BILLION ESCUDOS FOR 1975 WOULD NOT REQUIRE MOBILIZATION OF GOLD RESERVES. HE LISTED FOLLOWING RESOURCES AVAILABLE TO GOP: ESC. 14 BILLION OF REMAINING FOREIGN EXCHANGE RESERVES; \$250 MILLION STANDBY CREDIT FROM BIS (PART USED ALREADY--REST TO BE USED BY END OF YEAR); IMF GOLD TRANCHE AND OIL FACILITY (NEGOTIATIONS FOR DRAWINGS UNDERWAY); \$150 MILLION 5 YEAR STANDBY CREDIT WITH PRIVATE BANKS (NOT YET CALLED UPON). PORTUGUESE SAID POLICY RE POSSIBLE USE OF ESC 30 BILLION GOLD RESERVE (EVALUATED AT \$42.22 PER OUNCE) IN 1976 NOT YET DEFINED. GROUP DID NOT DISCUSS THIS PART OF PORTUGUESE PRESENTATION, BUT SECRETARIAT NOTED TEMPORARY WORKING PARTY OF ECONOMIC POLICY COMMITTEE OF OECD HAD SCHEDULED SEPTEMBER MEETING TO DISCUSS FINANCING PROBLEMS OF SMALLER COUNTRIES.

6. DISCUSSION OF TRADE MEASURES: PORTUGUESE DEL'S OPENING STATEMENT OUTLINED REASONS FOR CHOICE OF SURCHARGE (ADMINISTRATIVE EASE, AVOIDANCE OF PROBLEMS FOR INVISIBLES EARNINGS AND MACRO-POLICY THAT WOULD STEM FROM DEVALUATION, AVOIDANCE OF CREDIT PROBLEMS IF DEPOSIT SCHEME ATTEMPTED), AND SELECTIVITY (DESIRE TO AVOID PRICE INCREASES IN ESSENTIAL IMPORTS AND IN EXPORTS). REGARDING RATIONALE FOR LISTS, HE SAID 30 PERCENT ITEMS WERE MOSTLY LUXURY CONSUMER GOODS AND INTERMEDIATE GOODS FOR PRODUCTION OF NON-ESSENTIALS, WHILE 20 PERCENT GROUP INCLUDED CONSUMER APPLIANCES AND NON-ESSENTIAL ITEMS WHICH MIGHT BE REPLACED BY INTERNAL PRODUCTION. HE INDICATED ELIMINATION OF SURCHARGE AFTER END OF 1975

WOULD DEPEND UPON RESULTS ACHIEVED.

7. SEVERAL DELS NOTED UNEVEN DISTRIBUTION OF BURDEN OF SURCHARGE AMONG OECD MEMBERS AS RESULT OF SELECTIVITY. UK SAID ITS EXPORTERS WERE PARTICULARLY WORRIED ABOUT SURCHARGE AND ABOUT TREATMENT AFFORDED GOODS UNDERWAY AND ON ORDER. SWISS ECHOED THIS CONCERN, AND SWEDES SAID THEY REGRETTEED PORTUGUESE ACTIONS AND URGED APPROPRIATE INTERNAL MEASURES BE TAKEN. ALL DELS WHO LIMITED OFFICIAL USE

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SPOKE URGED EARLY ELIMINATION. US DEL FOLLOWED LINE IN REFTEL, EXPRESSING UNDERSTANDING FOR PORTUGUESE SITUATION AND NOTING POSSIBLE ADVERSE SIDE EFFECTS ON INTERNATIONAL TRADE CLIMATE.

8. IN RESPONSE TO SECRETARIAT INTERVENTION NOTING THAT SURCHARGE APPARENTLY HAD A PROTECTIVE AIM (VIA STIMULATION OF IMPORT-REPLACING PRODUCTION) AS WELL AS A

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GENERAL BOP OBJECTIVE, PORTUGUESE DEL ASSURED WORKING PARTY THAT PROTECTIVE ASPECT WAS A MINOR ONE, AND THAT GOP HAD NO INTENTION TO USE SURCHARGE TO EFFECT STRUCTURAL CHANGES. HE SAID EXEMPTIONS WOULD BE GRANTED IN CASES WHERE IMPORTERS OR MANUFACTURERS COULD DEMONSTRATE THAT DOMESTIC PRODUCTION COULD NOT BE EXPANDED IN VERY SHORT RUN. GROUP WAS PLEASED BY THIS ASSURANCE, GIVEN FACT THAT SURCHARGE COULD DOUBLE OR TRIPLE PROTECTION AFFORDED ECONOMY IN GENERAL AND COULD BE MUCH MORE SIGNIFICANT FOR PARTICULAR PRODUCTS.

9. COMMENT: JOINT EDRC/TCWP REVIEW PROVED QUITE EFFECTIVE IN GIVING OPPORTUNITY FOR EXPERT LEVEL BROAD-GAGED BROAD-GAUGED EXAMINATION OF PORTUGUESE ECONOMIC SITUATION AND MISSION FEELS THIS HAS SET GOOD PRECEDENT FOR APPROACH TO INCREASED SURVEILLANCE OF MEMBER COUNTRIES POLICIES IN FUTURE.

10. FOLLOW-UP: SECRETARIAT WILL DO INTEGRATED REPORT
OF JULY 11 CONSULTATIONS FOR TRANSMISSION TO COUNCIL.

11. FOR LISBON: FULL LIST OF PORTUGUESE DELEGATION
AND SET OF DOCUMENTS FOR MEETING BEING POUCHED TO
GRAHAM.

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